

**Illinois Department of Revenue
Regulations**

Title 86	Part 100	Section 100.3400	Apportionment of Business Income of Financial Organizations (IITA Section 304(c))
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TITLE 86: REVENUE

**PART 100
INCOME TAX**

Section 100.3400 Apportionment of Business Income of Financial Organizations (IITA Section 304(c))

- a) In general. *Business income of a financial organization shall be apportioned to this State by multiplying such income by a fraction, the numerator of which is its business income from sources within this State, and the denominator of which is its business income from all sources.* (IITA Section 304(c)(1))
- 1) IITA Section 304(c)(1) expressly provides that the adjusted income of an international banking facility is excluded from the amounts sourced to Illinois under its provisions. Adjusted income from an international banking facility is defined in IITA Section 304(c)(2) to mean amounts reported on a *Consolidated Report of Condition which is filed with the Federal Deposit Insurance Corporation on Schedule A, lines 2.c., 5.b. or 7.a.*, or any successor or substitute report required by the Federal Deposit Insurance Corporation, as applicable to the tax year in question. Accordingly, all references in this Section to items sourced to Illinois must be read to exclude items comprising the adjusted income of an international banking facility.
- 2) Any item of income that is excluded from base income or subtracted in the computation of base income of the financial organization must therefore be excluded from the formula. See *Continental Illinois National Bank and Trust Company of Chicago v. Lenckos*, 102 Ill.2d 210 (1984). For example, dividends deducted from federal taxable income under 26 USC 243 or subtracted in the computation of base income under IITA Section 203(b)(2)(O) are excluded from the apportionment formula.
- 3) In determining the amount of business income included in the numerator or the denominator of the apportionment fraction, amounts of business income received during the tax year shall not be reduced by any expenses allocable to the business. The determination of gains or losses included in business income shall take into account the taxpayer's basis in property sold or otherwise disposed of, but in no event shall a loss included in business income reduce the numerator or denominator of the apportionment fraction below zero.
- b) Definitions. For purposes of this Section, the following definitions shall apply:

- 1) Customer. A "customer" is a person for whom the financial organization provides financial services directly or through an agent or other fiduciary of the financial organization. Illustrative examples of this definition include:
 - A) In the case of a bank participating in a syndicated loan, the borrower is a customer of the bank if the bank is a named party to the original transaction for whom the lead bank is acting as agent. However, if a bank purchases a participation in an existing loan, the borrower is not a customer of the bank because the bank is not providing a financial service to the borrower.
 - B) In the case of a financial organization financing the accounts receivable of a business, the obligor on the account is a customer of the financial organization only if the financial organization purchases the receivable, thus creating a direct relationship between itself and the obligor.
 - i) Example 1: If a financial organization makes a loan to a company secured by the company's customer receivables, the company is the customer of that financial organization but the company's customers are not customers of the financial organization because the loan is a financial service provided to the company rather than to the company's customers.
 - ii) Example 2: If a financial organization purchases a customer account receivable from a company, the company's customer thereby becomes a customer of the financial organization.
 - C) A financial organization purchases a publicly-traded security of an issuer for whom the organization provides financial services. If the purchase is unrelated to any financial services provided by the financial organization to the issuer, the issuer is not a customer of the financial organization for purposes of sourcing the income derived from the security. If, however, the purchase of the security is made in connection with a financial service provided to the issuer as a customer of the financial organization, the issuer is a customer for sourcing the income derived from the security.
- 2) Dividend. "Dividend" means any item defined as a dividend under 26 USC 316 and any other item of income characterized or treated as a dividend under the Internal Revenue Code.
- 3) Fees, commissions or other compensation for financial services. "Fees, commissions or other compensation for financial services" means all items of income, other than interest, dividends and gross profit from trading in stocks, bonds or other securities, paid to a financial organization by its customers for the provision of those services characteristic of financial organizations, as defined in Section 100.9710 of this Part. Such items include, to the extent received for services characteristic of a financial organization:
 - A) Late payment fees or penalties to the extent not properly characterized as interest;

- B) Penalties for early withdrawal of deposits or early repayment of debt; and
 - C) Loan origination fees, charges for credit investigations, filing fees, etc., to the extent not properly characterized as interest.
- 4) Gross profits from trading in stocks, bonds or other securities. "Gross profits from trading in stocks, bonds or other securities" of a financial organization means the net gain or net loss realized on the sale, exchange or other disposition of a security other than a security representing an interest in or obligation of that financial organization. Gross profits from trading in stocks, bonds or other securities do not include any amount that is properly characterized as a fee or commission of the financial organization for the transaction or as interest or dividends. Gross profits from trading in securities do include any net gain or loss realized on the sale, exchange or other disposition of some or all of a financial organization's interest in a loan or other indebtedness of a customer of the financial organization payable to the financial organization.
- 5) Illinois customer. "Illinois customer" means:
- A) A customer who is an Illinois resident individual, trust or estate; or
 - B) A customer other than an individual, trust or estate whose commercial domicile is in Illinois.

Unless a financial organization has actual knowledge that the residence or commercial domicile of a customer during a taxable year is in a state other than the state in which the customer's billing address is located, the customer shall be deemed to be an Illinois customer if the billing address of the customer, as shown in the records of the financial organization relating to the interest income being sourced, is located in Illinois and shall be deemed not to be an Illinois customer if that billing address is located outside Illinois.

- 6) Interest. "Interest" means "compensation for the use or forbearance of money". See *Deputy v. du Pont*, 308 U.S. 488, 498 (1940).
- A) Interest does not include late payment penalties that are in addition to interest expressly charged on any past-due balance or that are computed without regard to the amount of the past-due balance or the length of time a payment is late.
 - B) Interest includes the amortization of any discount at which an obligation is purchased and is net of the amortization of any premium at which an obligation is purchased. Any amount in excess of the purchase price received in payment of an obligation purchased at an arm's-length discount shall be rebuttably presumed to be interest.
 - C) Interest includes any amount received upon the sale, exchange or other disposition of an obligation to the extent that such amount represents the

accrual of interest on the unpaid balance of the obligation since the most recent payment made on that obligation.

- 7) Margin account. "Margin account" means any extension of credit made by a financial organization for the purchase or carrying of securities by the borrower, within the meaning of 15 USC 78g.
 - 8) Stocks, bonds or other securities. "Stocks, bonds or other securities" means any share of stock in any corporation, certificate of stock, or interest in any corporation, note, bond, debenture, or other evidence of indebtedness, or any evidence of an interest in or right to subscribe to or purchase any of the foregoing, within the meaning of 26 USC 1236(c).
- c) Sourcing rules. For the purposes of this Section, business income (other than the adjusted income of an international banking facility) of a financial organization from sources within this State is the sum of the following amounts:
- 1) *Fees, commissions or other compensation for financial services rendered within this State.* (IITA Section 304(c)(1)(A))
 - A) Scope. This subsection (c)(1) applies to all payments received by a financial organization from its customers for services characteristic of a financial organization, except to the extent the payment is sourced according to subsection (c)(2), (c)(3) or (c)(4) of this Section.
 - B) Application. Financial services are "rendered within this State" if:
 - i) The income-producing activity is performed in this State; or
 - ii) The income-producing activity is performed both within and without this State and a greater proportion of the income-producing activity is performed within this State than without this State, based on performance costs.
 - iii) If the performance costs of two or more income producing activities cannot readily be allocated among those activities, the gross income resulting from those activities shall be combined and sourced to Illinois using the combined performance costs for all those activities.
 - 2) *Gross profits from trading in stocks, bonds or other securities managed within this State.* (IITA Section 304(c)(1)(B))
 - A) Scope. This subsection (c)(2) applies only to net gains or losses realized on the sale or exchange of securities. Dividends received on stocks and interest received on securities are sourced pursuant to subsection (c)(3) of this Section.
 - B) Application. The trading of a stock, bond or other security is "managed within this State" if:

- i) The income producing activity is performed in this State; or
 - ii) The income producing activity is performed both within and without this State and a greater proportion of the income producing activity is performed within this State than without this State, based on performance costs.
 - iii) If the performance costs of two or more income producing activities cannot readily be allocated among those activities, the gross income resulting from those activities shall be combined and sourced to Illinois using the combined performance costs for all those activities.
- 3) *Dividends and interest from Illinois customers, which are received within this State.* (IIITA Section 304(c)(1)(C))
 - A) Scope. This subsection (c)(3) applies to all dividends included in business income of the financial organization and to all interest (other than interest on margin accounts, which is sourced under the provisions in subsection (b)(4) of this Section) received by the financial organization.
 - B) Application. Interest is never sourced to Illinois under this subsection (c)(3) unless it is received from an Illinois customer. Interest from an Illinois customer or dividends are "received in this State" if the payment comes within the control of the financial organization or of an agent or other fiduciary of the financial organization at a location within the State of Illinois. If payment of an item of interest income that has been accrued and included in base income for a tax year is not received prior to the date the return for that tax year is filed, the financial organization shall treat the payment as received at the location to which the borrower is directed to send the payment or, if no single location is specified, at the location at which the financial organization reasonably expects to receive the interest. The following examples illustrate the principles for determining when a payment comes within the control of a financial organization:
 - i) Example 3: A financial organization directs its customers in the Midwest to mail all payments to a lock box located in Detroit. Interest and dividend payments mailed to the Detroit lock box are received in Detroit. Such payments are received in Detroit even if the checks are first deposited by or on behalf of the financial organization in a bank located outside Detroit because the checks come within the control of the financial organization's agent when received at the lock box. Whether the lock box is serviced by the financial organization's own employees or by a company acting as agent for the financial organization is irrelevant, because receipt by either an employee or an agent of the financial organization will give it control.

- ii) Example 4: An electronic transfer of funds is received by a financial organization at the location of the bank carrying the account of the financial organization into which the funds are deposited. In the case of a bank with branches in both Illinois and Missouri, whose Federal Reserve Bank account is maintained at the Federal Reserve Bank of St. Louis, an electronic transfer via the Federal Reserve is received by the bank in St. Louis, the location of its account. In the case of a financial organization receiving an electronic transfer via the Federal Reserve through that bank, the payment is received at the branch of the bank in which the financial organization's account is maintained because the payment is not within the financial organization's control until deposited into its account by its bank. The deposit of funds into the account of the bank at the Federal Reserve Bank does not place the funds within the control of the financial organization because the bank, merely by participating in the electronic transfer, is not acting as collection agent for the financial organization.
 - iii) Example 5: A credit card bank purchases its cardholders' balances from a retailer pursuant to an agreement under which the retailer services the accounts. Payments are received by the credit card bank at the location where the retailer receives the payments on its behalf, not at the location to which the retailer forwards the payments.
 - iv) Example 6: A bank makes a loan to an Illinois customer secured by the customer's accounts receivable. Pursuant to the loan agreement, the bank's customer directs its customers to send their payments to the bank, which deposits the payments in an account at its Chicago branch in the name of the customer, from which the bank may withdraw loan payments to itself. The funds in the customer's account are not within the control of the bank. Payments withdrawn by the bank from the account at the Chicago branch pursuant to the agreement are received in Illinois regardless of where the payments from the customers are received by the bank. However, if the customer pays the bank by check drawn on the account at the Chicago branch, payment is received by the bank in the state in which it receives the check.
- 4) *Interest charged to customers at places of business maintained within this State for carrying debit balances of margin accounts, without deduction of any costs incurred in carrying such accounts. (IITA Section 304(c)(1)(D))*
 - A) Scope. This subsection (c)(4) applies to all interest on margin accounts.
 - B) Application. Interest on a margin account is sourced to this State if the financial organization's place of business through which the borrower ordinarily conducts business with the financial organization is located within Illinois.

- 5) *Any other gross income resulting from the operation as a financial organization within this State.* (IITA Section 304(c)(1))
- A) Scope. This subsection (c)(5) rule applies to every item of business income of a financial organization that is not governed by subsections (c)(1) through (c)(4) of this Section.
 - B) Application. Gross income that results from the operation of a taxpayer as a financial organization "within this State" is allocable to this State if:
 - i) The income producing activity is performed in this State; or
 - ii) The income producing activity is performed both within and without this State and a greater proportion of the income producing activity is performed within this State than without this State, based on performance costs.
 - iii) If the performance costs of two or more income producing activities cannot readily be allocated among those activities, the gross income resulting from those activities shall be combined and sourced to Illinois using the combined performance costs for all those activities.

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